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Accounts may not be answer to questions about system

By William M. Welch, USA TODAY

WASHINGTON — President Bush is selling private investment accounts, financed with a share of current payroll taxes, as a way to solve Social Security's long-range financing problems and benefit younger workers. (**Related story**: Bush: It's time to fix Social Security)

But experts who have studied the complex national retirement and insurance program say creating private accounts alone won't shore up the system. Raising taxes could ensure its solvency, but the president has ruled that out.

The other way is to cut future benefits, and with it the money Social Security will pay out to future retirees. Cutting guaranteed benefits is what most private-account proposals do — though advocates don't advertise that feature.

Bush has not offered a specific proposal for Social Security. But in his economic forum that ended Thursday — a pep rally for privatization — Bush made creation of private accounts one of three principles that he believes any plan before Congress next year must adhere to. The others: no increase in payroll taxes that fund Social Security, and no cut in benefits to those already retired or about to retire.

The president and his party recognize that "private ownership" of Social Security investment accounts is a powerful idea with particular appeal to younger workers.

"These personal accounts, I would say, are a critical part of any solution," Treasury Secretary John Snow said in an interview. "They provide people with this ability to earn higher rates of return than otherwise would be available on their investment in Social Security. This opportunity to earn a higher rate of return is pretty attractive."

Democratic critics of private accounts in Social Security are trying to counter that appeal by focusing on what they say is the downside of the deal. They say that implicit in creating private

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investment accounts is a reduction in future Social Security benefits from the levels guaranteed in present law.

What accounts would mean

This hypothetical example and projections are from the most conservative of the three investment-account proposals made by the 2001 President's Commission to Strengthen Social Security.

Where the system stands now:

Current payroll tax is 12.4%. Workers and employers each pay 6.2%.

Projections indicate that Social Security outlays will exceed income in 2018, and the fund will become insolvent in 2042.

Bringing Social Security into balance over 75 years could require a 15% increase in payroll taxes, a 13% cut in benefits, or some combination.

How the system changes under one commission proposal:

Workers would contribute 2% of their wages to a personal account and 4.2% to the Social Security trust fund. Employers would continue to pay their 6.2% match to the trust fund.

On retirement, workers would receive a reduced benefit from Social Security but, in theory, a higher total benefit when investments are included (see chart below).

The proposed plan would cost an undetermined amount in "transition" costs as taxes used to pay benefits to current retirees are diverted to personal accounts.

Projected annual benefits in 2052 (in 2001 dollars):

	Low wage-earners	Medium wage-earners	High wage-earners
Under current plan	$11,832	$19,536	$25,812
Under proposal {+1} with investment account	$12,888	$21,864	$29,544

1 — Assumes traditional benefits would be cut about 25% and personal accounts would grow at the rate of inflation plus 3.5% a year.

Sources: President's Commission to Strengthen Social Security, 2001; Social

That may or may not prove a good bet for individual workers. Either way, opponents argue, diverting a portion of today's workers' payroll taxes into private accounts takes money out of Social Security's revenue stream, which will hurt rather than help its long-term financial solvency.

"This actually makes the problems worse," said Rep. Robert Matsui, D-Calif., top Democrat on the House Social Security subcommittee. "The president, by doing this, actually cuts 10 years off of the life of the Social Security system. This plan makes no sense at all."

Neither Bush nor Republican leaders in Congress have said how much in payroll taxes they want to divert from the benefit stream into private accounts. Proposals by Bush's own 2001 study commission and others have centered on 2% to 4% of salary. That may sound small, but it represents nearly one-third to two-thirds of the 6.2% payroll tax that employees pay into Social Security. Employers match that payment for a total 12.4% per worker, up to a maximum of $87,900 in income this year. That cap rises to $90,000 next year.

Under the most talked-about plan from Bush's commission, the growth in future benefits would be reduced by calculating them based on the growth of prices rather than wages. That change alone would ensure the system is solvent for 75 years.

White House spokesman Scott McClellan,

Security Board of Trustees report, 2004.

responding to Democrats, said projected financial shortfalls call into question whether future benefits can be paid unless the system is overhauled.

"There are no guaranteed benefits right now. That's an empty promise," McClellan said. "Younger workers will not have the benefits that they are owed under the current Social Security system."

Social Security is a pay-as-you-go system. Today, it's taking in more money that it pays in benefits. The extra money is put into the Social Security Trust Fund in exchange for government bonds. The federal government then uses that money for other programs.

Assuming the government made good on its Treasury bonds — and it always has — Social Security would have enough revenue to pay 100% of benefits until 2042. After that, the program would have enough money to cover only about 70% of scheduled benefits.

Alicia Munnell, director of the Center for Retirement Research at Boston College and a former Clinton administration adviser, said in a report this month that only by changing Social Security's cash flow could that future imbalance be fixed. "The only ways to improve cash flows are to increase revenues or decrease benefits," she said. "Private accounts, which divert payroll taxes to private-sector investments, by themselves do nothing to improve cash flows."

But she added: "Private accounts might be a device to improve the political chances of cutting future benefits."

Sen. Jon Corzine, D-N.J., former chairman and CEO of Goldman Sachs investment firm, dismissed the idea that investing individuals' Social Security accounts on Wall Street would bring big rewards. Bush's forum, he said, had "no discussion of the deep, long-term cuts that will come in benefits" with a private-accounts plan.

Much of the coming debate in Congress will center on how Bush would keep benefits flowing to today's retirees if a portion of today's workers' payroll taxes is diverted to their own private accounts. The administration intends to borrow that amount, estimated at about $2 trillion. It wants to avoid adding it to the federal debt, which now tops $7.5 trillion, so it has come up with the euphemism "short-term transitional funding."

Even that borrowing would not shore up the program, however, because it would only replace money the system would take in through payroll taxes if there were no change.

Contributing: Barbara Hagenbaugh and Judy Keen


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